VZCZCXYZ0000
RR RUEHWEB

DE RUEHSI #0198/01 0480725
ZNR UUUUU ZZH
R 170725Z FEB 10
FM AMEMBASSY TBILISI
TO RUEHC/SECSTATE WASHDC 2862
INFO RUEATRS/DEPT OF TREASURY WASHINGTON DC
RUCPDOC/DEPT OF COMMERCE WASHINGTON DC

UNCLAS TBILISI 000198

DEPT FOR EUR/CARC, EEB/IFD, N. Hatcher, G. Hicks
PLEASE PASS TO USTR P. Burkhead, J. Kallmer

SIPDIS

SENSITIVE

E.O. 12958: N/A
TAGS: EINV EFIN ETRD ELAB KTDB PGOV

SUBJECT: GEORGIA: INVESTMENT CLIMATE STATEMENT FOR 2010

REF: 09 STATE 124006

¶1. Per reftel, below is Embassy TbilisiQs Investment Climate Statement for submission for 2009.

Introduction

Since 2004,, the Georgian Government has undertaken an ambitious program to modernize and liberalize its economy. Institutional reforms include restructuring and downsizing government ministries, privatizing large state-owned entities, increasing public servant salaries, reducing the number and rates of taxes, improving tax and fiscal administration, streamlining licensing requirements, simplifying customs and border formalities, and generally undertaking efforts to make it easier to do business in Georgia. The current Georgian leadership views liberal market economies like Singapore and Dubai as models for economic growth. Prior to the August 2008 war with Russia and the global financial crisis, the Georgian economy had experienced multiple years of double-digit growth. Despite the dual shock, the Georgian economy grew by 2.1 percent in 2008. In 2009, the Georgian economy contracted by four percent.

In 2009, Georgia moved from 18 to 16 on the World BankQs QDoing Business Report.Q In 2010, Georgia moved from 16 to 11. The report measures business regulations and their enforcement across 183 economies. The report states that QGeorgia eased the process for dealing with construction permits by introducing simplified, risk-based approval processes and new time limits. The documentation requirements for import and export were simplified, and there was a significant decrease in the cost of trade.Q Georgia tops the rankings for the region.

IFCQs 2009 report singled out the areas of Starting a Business, Registering Property, Getting Credit and Paying Taxes as GeorgiaQs priority achievements. In addition, new regulations guarantee the right of borrowers to inspect their data at a private credit bureau, helping to improve the quality and accuracy of credit information. Amendments to the civil code, effective December 2007, address secured transactions, allowing parties to a security agreement to agree to out-of-court enforcement of the creditorQs security rights at the time the parties sign the security agreement. The corporate income tax rate was reduced from 20 percent to 15 percent, and the social tax abolished. A new online business registry makes it easier to register property by eliminating the requirement for legal entities to obtain several pre-registration documents. This reform reduced the number of procedures required to transfer a title from five to two, and the time from five days to three. Registration fees were also reduced. Finally, amendments to the Law on Entrepreneurs made it easier to start a company by eliminating the requirements for minimum capital, a company seal and a company charter and by making the use of notaries optional.

In the 2008 Report, The World Bank credited Georgia for strengthening investor protections with amendments to its securities law which

eliminated loopholes allowing corporate insiders to expropriate minority investors. Georgia adopted a new insolvency law shortening timelines for reorganization of a distressed company or disposition of a debtor's assets. The law shortened the approval process for construction permits and simplified procedures for registering property. It made starting a business easier by eliminating capital requirements. In addition, the country's private credit bureau added payment information from retailers, utilities and trade creditors to Qpayment information from retailers, utilities and trade creditors to the data it collects and distributes.

Georgia scored high in the Heritage Foundation/ Wall Street Journal 2009 Economic Freedom Report. This index measures 162 countries across ten specific factors: Business Freedom, Trade Freedom, Fiscal Freedom, Freedom from Government, Monetary Freedom, Investment Freedom, Financial Freedom, Property Rights, Freedom from Corruption, and Labor Freedom. Georgia's economic freedom score is 69.8, making its economy the 32nd QfreestQ in the 2009 Index. Its overall score is 0.5 points higher than 2008 due to improvements in business freedom, trade freedom and freedom from corruption. Georgia's economy is qualified under the category of 'moderately free', along with Spain, Austria, Norway, the Slovak Republic, and the Czech Republic. Georgia is ranked 19 out of 43 countries in the European region, and its overall score is equal to the European regional average. According to the report, Georgia scored high in business freedom, fiscal freedom, freedom from government, investment freedom, and labor freedom, but scored below the average in the areas of property rights protection and corruption.
Judicial corruption remains a problem despite substantial improvement in efficiency and fairness in the courts. Both foreigners and Georgians continue to question the judicial system's ability to protect private property and contracts. The enforcement of laws protecting intellectual property rights is inadequate. However, the World BankQs QAnti-Corruption in Transition 3Q report places Georgia among the countries showing the most dramatic improvement in the fight against corruption, due to implementation of a strong program of economic and institutional reform.
Georgia also significantly improved in Transparency International's (TI) annual Corruption Perceptions Index. The index scores countries on a scale from zero (perceived to be highly corrupt) to ten (perceived to have low levels of corruption). Out of the 180 countries surveyed in 2009, Georgia ranked 66th, moving from 67 in 2008. In its 2009 report, TI concludes, Qpetty corruption has been reduced significantly in Georgia. However, concerns remain regarding high-level corruption and on corrupt practices in the judiciary.Q
The Georgian GovernmentQs fiscal and monetary policies have created a relatively stable macro-economic environment. However, in 2009, the realities of the global financial crisis and the aftermath of the 2008 conflict meant the government had to focus on job creation and stimulating the economy. In 2009 the economy contracted by four percent, following growth of 2.1 percent (2008) and 12.4 percent (2007). Estimated growth for 2010 stands at two percent.

Inflation for 2009 totaled three percent, a significant drop from inflation of ten percent in 2008. This decrease was largely due to the economic slowdown. Hoping for economic recovery, the Government has projected inflation for 2010 at six percent.

The Georgian lari has remained relatively stable despite multiple economic shocks. Following the August 2008 crisis, the lari moved from 1.4 lari to the dollar to 1.65 lari to the dollar. Though it fluctuated slightly, the lari remained at approximately 1.67 lari to the dollar throughout 2009. The Georgian Government manages the currency, and has intervened, for example after the 2008 conflict, to stop the currency from devaluation.

Based on the economyQs overall performance and the Georgian governmentQs strong commitment to structural changes, Georgia received its first sovereign credit rating in late 2005 from Standard and PoorQs (S&P) - a QB+Q long term and a QBQ short term. In September 2009, the S&P long-term/short-term credit rating for the Government of Georgia were QB/BQ with a QstableQ ratings forecast. The estimated risk of transfer and converting of currency for Georgian non-sovereign borrowers is "B/B-". In its analysis, S&P notes a potential risk to the economy once assistance pledged following the 2008 conflict (estimated at USD 5.7 billion) has been disbursed. Fitch currently rates Georgia, which launched its debut $500 million Eurobond in spring 2008, as QB/B-Q with a stable outlook. In August 2009, Fitch Ratings affirmed GeorgiaQs Long-Term Foreign Currency (FC) and Local Currency

(LC) Issuer Default Ratings at QB+Q, removing them from Rating Watch Negative and assigning stable outlooks. At the same time, Fitch upgraded GeorgiaQs Country Ceiling to QB/B-Q from QB+Q. In upgrading Georgia, Fitch noted GeorgiaQs GDP per capita and level of human development is significantly higher than the QBQ range median. It has a favorable business climate and record of structural reforms, underscored by its ranking in the World BankQs Doing Business Survey. Over the medium term, Georgia has a promising growth model in its favorable business climate, based on low tax rates, light regulation, and low corruption; its investment in infrastructure and transport links; and its high human capital-to-wage ratio.

In November 2009, President Saakashvili presented an QAct on Economic QIn November 2009, President Saakashvili presented an QAct on Economic FreedomQ to the parliament. The aim of this act is to codify GeorgiaQs economic reforms, and the governmentQs commitment to a liberal economy, in the countryQs constitution. The act envisages a minimal state role in the economy, creates legislative guarantees for business, and bans the introduction of new licenses and permits. The act also amends the constitution to limit the maximum ratio of budgetary expenditures to GDP at 30 percent, budget deficit as a percent of GDP at 3 percent, and debt-to-GDP ratio at 60 percent. In addition, taxes will only be increased if approved through a public referendum.

Georgia became a member of the World Trade Organization in 2000. The WTOQs first report on the trade policies and practices of Georgia, published in December 2009, noted the success of the countryQs economic policies. The WTO particularly highlighted GeorgiaQs pace of reform and the countryQs reliance on the private sector to spur development. According to the report, continuing structural reforms will be the key to strengthening GeorgiaQs resilience to shocks, sustaining growth, attracting investment into export activities, and improving productivity.

Despite improvements to the economy, Georgia still lags in many areas important to investors. More than 25 percent of the population live below the poverty line and many still rely on subsistence agriculture. Greater familiarity with western business practices and legal norms is required. While physical infrastructure, such as road networks, improved significantly from 2005 to 2009, much remains to be done, especially in rural areas. Most natural gas for heating and electricity generation is imported. In a relatively short period, however, Georgia has become a net exporter of electricity, selling

power in Turkey, Russia and throughout the Caucasus. The rehabilitation of existing power plants and the development of new ones, together with the costruction of new high voltage electricity lines to connected Georgia to Turkey, should ensure Georgia remains a key player in the regional electricity trade.

The main source of sustained future economic growth will be private investment, both domestic and foreign. The governmentQs challenge is to implement existing legislation, continue the fight against corruption, defuse tensions in the separatist regions, and undertake new reforms in order to increase investor confidence.

Georgia receives assistance from the United States, the European Union, and a range of international institutions. U.S. assistance has focused on promoting democratic development and free media, developing rule of law, good governance and the administration of government economic and financial institutions, improving critical physical infrastructure, enhancing private sector competitiveness, and promoting the growth of a free market economy. In 2006, GeorgiaQs clear-cut commitment to reform earned it one of the first compacts with the U.S. Millennium Challenge Corporation, which has provided investments in infrastructure, tourism, and agriculture.

After the August 2008 conflict with Russia, foreign donors committed USD 4.5 billion to help Georgia recover from direct and indirect war damage. According to the World Bank-led international needs assessment for Georgia, the major impact of the conflict was on the investment and consumer climate, which led to a sharp economic drop in FDI and GDP. The United States committed USD 1 billion in assistance to assist in repairing damaged infrastructure and help the Georgian economy recover from the economic shock of the war.

President Saakashvili and his government have strengthened GeorgiaQs bilateral relations with many countries, reaching out to Ukraine,

Turkey, Italy, Poland, Latvia, Lithuania, Estonia, Japan, Kazakhstan, the UK, Germany, the Netherlands, and the United States. Georgia has a partnership agreement with the European Union and an action plan for reform to allow a closer relationship. Georgia maintains the goal of eventual membership in the European Union. Georgia is one of only fifteen countries in the world that benefit from GSP+ access to the EU market, allowing duty-free access for more than 7,000 products. It is making an effort to harmonize its regulatory environment with international standards, particularly those established by the EU, and is pursuing a free trade agreement with the EU. Georgia enjoys duty-free trade with other former Soviet Union countries. It benefits from preferential trading relationship with the United States, Turkey, Canada, Switzerland, and Japan. In 2007, Georgia signed a free trade agreement with Turkey, as well as a Trade and Investment Framework Agreement and an Open Skies Agreement with the United States.

Georgia is located at the crossroads between Europe and Asia. It is the shortest route from Central Asia to Europe, and could be a north-south bridge between Turkey and the Russian Federation. Georgia has two deep-water ports on its Black Sea coast, Poti and Batumi. Labor costs in Georgia are comparable to the Far East, while transit time for shipment of goods to Europe is far less. The government has launched an extensive road rehabilitation project aimed at upgrading Qlaunched an extensive road rehabilitation project aimed at upgrading the road quality and constructing new facilities to improve communication infrastructure. The government allocated USD 310 million for road rehabilitation projects in 2009 and projected around USD 420 million in 2010. The governments of Turkey, Azerbaijan, and Georgia have agreed to construct a rail link from Kars, Turkey through Georgia to Baku, Azerbaijan. Freight from Europe will then be transported through Turkey to Baku via Tbilisi and then to Central Asia from Baku by ferry. Ongoing construction of a tunnel under the Bosphorus in Istanbul will allow freight to travel from Georgia directly into Europe. In addition, Georgia is improving its network of rail-ferry connections with Black Sea countries, including Ukraine, Romania, and Turkey, which will further increase transportation and trade turnover with these countries.

GeorgiaQs relations with its northern neighbor Russia have been problematic. In 2005 and 2006, Russia banned imports of Georgian agricultural products, mineral water, and wine. At the time, Russia was the largest importer of Georgian products. These restrictions continue in 2010. In September 2006, Russia cut all direct transport links with Georgia. Gazprom, the Russian gas monopoly, quadrupled the price of natural gas supplied to Georgia over two years. Despite these actions, the Georgian economy has continued to grow. Georgian businesses have diversified markets and continue to actively seeking new markets for Georgian products and new sources of imports, especially in Ukraine, the Baltics, and Central Europe. Georgia has diversified its energy supplies, purchasing natural gas from Azerbaijan and increasing its own hydroelectric generating capacity.

Openness to Foreign Investment

Georgia is open to foreign investment and is eager to welcome new investors. The country is currently implementing an aggressive marketing campaign to encourage foreign investment, and is developing a regulatory framework intended to foster competition. Legislation governing foreign investment establishes favorable conditions, but not preferential treatment, for foreign investors. The Law on Promotion and Guarantees of Investment Activity protects foreign investors from subsequent legislation that alters the condition of their investments for a period of ten years.

The U.S.-Georgia Bilateal Investment Treaty, in force since 1994, guarantees U.S. investors national treatment or most favored nation treatment, whichever is better, in the establishment, operation, and sale of their investments. Exceptions to national treatment may be made by Georgia for investments in maritime fisheries; air and maritime transport and related activities; ownership of broadcast, common carrier, or aeronautical radio stations; communications satellites; government-supported loans, guarantees, and insurance; and landing of submarine cables.

Legislation governing foreign investment includes the Constitution, the Civil Code, the Tax Code, and the Customs Code. Other relevant legislation includes the Law on Entrepreneurs, the Law on Promotion and Guarantees of Investment Activity, the Bankruptcy Law, the Law on

Courts and General Jurisdiction, the Law on Limitation of Monopolistic Activity, the Accounting Law, and the Securities Market Law.

Georgia has negotiated 39 agreements for avoidance of double taxation, of which 24 have entered into force. The active agreements are with Uzbekistan, Azerbaijan, Ukraine, Romania, Bulgaria, Turkmenistan, Armenia, Kazakhstan, Iran, the Netherlands, Greece, Italy, Belgium, Lithuania, Latvia, United Kingdom, China, Austria, Poland, Czech Republic, Germany, Finland, Denmark, and Estonia. Until the treaty with France enters into force upon ratification by France, a similar agreement signed by the USSR governs the issue. Eight treaties (including the aforementioned with France, Ireland, Kuwait, Luxemburg, Malta, Russia, Singapore, and Turkey) have been signed and are awaiting ratification by the parliaments of the respective countries. An agreement with Russia was signed in 1999 and ratified by the Georgian parliament in 2000. It has not been ratified by the Russian Duma, but Russia regards it as an active agreement. Negotiations are ongoing with Hungary, Israel, Slovenia, Spain, Switzerland, Kyrgyzstan and Cyprus. Agreements with Israel and Spain are expected to be signed in ¶2010.

The legal framework governing the ownership and privatization of property is established by the following acts: the Civil Code, the Law on Ownership of Agricultural Land, the Law on Private Ownership of Non-Agricultural Land, the Law on Management of State-Owned Non-Agricultural Land, and the Law on Privatization of State Property. Property rights in the extractive industries are governed by the Law on Concessions, the Law on Deposits, and the Law on Oil and Gas. Intellectual property rights are protected under the Civil Code and by the Law on Patents and Trademarks. Financial sector legislation includes the Law on Commercial Banks, the Law on National Banks, and the Law on Insurance Activities.

Georgia does not screen foreign investment in the country, other than imposing a registration requirement and certain licensing requirements Qimposing a registration requirement and certain licensing requirements as outlined below. Foreign investors have participated in most of the major privatizations of state-owned property. Transparency of such privatizations has at times been an issue, however. No law specifically authorizes private firms to adopt articles of incorporation which limit or prohibit foreign investment.

In 2005, registration of businesses was simplified. Paperwork and fees were reduced and processing time shortened. The government proudly promotes that an entrepreneur can start a business in three days. All companies are required to register with the Ministry of Finance, providing foundersQ and firm principals' names, dates and places of birth, occupations, and places of residence; incorporation documents; area(s) of activity; and charter capital. This information is made public and any person may request and review such information. Business registration and tax registration are separate procedures handled by the same department within the Ministry of Finance.
The Government of Georgia has privatized the majority of the largest formerly state-owned enterprises in the country. Successful privatization projects include major deals in energy generation and distribution, telecommunications, water utilities, port facilities, real estate assets, etc. By the end of 2009, the government announced a new wave of privatization, which includes railway, telecommunication, and utilities. A list of entities available to be privatized can be found on the website www.privatization.ge. Information on investment conditions and opportunities can be obtained from the Georgia National Investment and Export Promotion Agency, e-mail: info@investingeorgia.org, www.investingeorgia.org. Further information is available at a website maintained by the American Chamber of Commerce in Georgia, www.investmentguide.ge.
In 2005, 84 percent of existing licensing requirements were eliminated and a Qone stop shopQ for licenses was created. By law, the government has 30 days to make a decision, and if no reasonable ground for rejection is stated by the licensing authority within that time, the license or permit is deemed to be issued. Licenses are only required for activities that affect public health, national security, and the financial sector. Licensing currently is required in the following areas: weapons and explosives production, narcotics, poisonous and pharmaceutical substances, exploration and exploitation of renewable or non-renewable substances, exploitation of natural resource deposits, establishment of casinos and gambling houses and the organization of games and lotteries, banking, insurance, trading in securities, wireless communication services, and the establishment of radio and

television channels. The law requires the state to retain a controlling interest in air traffic control, shipping traffic control, railroad control systems, defense and weapons industries, and nuclear energy. Only the state may issue currency, banknotes, and certificates for goods made from precious metals, import narcotics for medical purposes, and produce control systems for the energy sector.

Conversion and Transfer Policies

Georgian law guarantees the right of an investor to convert and repatriate income after payment of all required taxes. The investor is also entitled to convert and repatriate any compensation received for expropriated property. Moreover, Georgia has accepted the obligations of Article VIII, Sections 2, 3, and 4 of the IMF Articles of Agreement, effective as of December 20, 1996. IMF members accepting the obligations of Article VIII undertake to refrain from imposing restrictions on payments and transfers for current international transactions and from engaging in discriminatory currency arrangements or multiple currency practices without IMF approval. By accepting the obligations of Article VIII, Georgia gives confidence to the international community that it will pursue sound economic policies that will obviate the need to use restrictions on the making of payments and transfers for current international transactions.

Under the U.S.-Georgia Bilateral Investment Treaty, the Georgian government guarantees that all transfers relating to a covered investment by U.S. investors can be made freely and without delay into and out of Georgia.

Foreign investors have the right to hold foreign currency accounts with authorized local banks. The sole legal tender in Georgia is the lari (GEL), which is traded on the Tbilisi Interbank Currency Exchange and in the foreign exchange bureau market. There is no difficulty in obtaining foreign exchange or significant delays in remitting funds overseas through normal channels. Several Georgian banks participate in the SWIFT and Western Union interbank communication networks. Businesses report that it takes a maximum of three days to transfer money abroad. There are no known plans to change remittance policies. Travelers must declare at the border currency and securities in their possession valued at more than GEL 30,000 (USD 17,341).

Expropriation and Compensation

The Georgian Constitution protects ownership rights, including
QThe Georgian Constitution protects ownership rights, including
ownership, acquisition, disposal, or inheritance of property. Foreign citizens living in Georgia possess rights and obligations equal to those of the citizens of Georgia. The Constitution allows restriction or revocation of property rights only in cases of extreme public necessity, and then only as allowed by law.

The Law on Procedures for Forfeiture of Property for Public Needs establishes the rules for expropriation domain in Georgia. The law allows expropriation for certain enumerated public needs. It provides a mechanism for valuation and payment of compensation, and for court review of the valuation at the option of any party. The Georgian law on investment allows expropriation of foreign investments only with appropriate compensation. Recent amendments to the expropriation law allow payment of compensation with property of equal value as well as money. Compensation includes all expenses associated with the valuation and delivery of expropriated property. Compensation must be paid without delay and must include both the value of the expropriated property as well as the loss suffered by the foreign investor as a result of expropriation. The foreign investor has a right to review an expropriation in a Georgian court. In 2007, Parliament passed a law generally prohibiting the government from contesting the privatization of real estate sold by the government before August 2007. The law is not applicable to certain enumerated properties.

The U.S.-Georgia Bilateral Investment Treaty permits expropriation of covered investments only for a public purpose, in a non-discriminatory manner, upon payment of prompt, adequate and effective compensation, and in accordance with due process of law and general principles of fair treatment.

Dispute Settlement

Georgian investment law allows disputes between a foreign investor and

a governmental body to be resolved in Georgian courts or at the International Center for the Settlement of Investment Disputes (ICSID), unless a different method of dispute settlement is agreed upon between the parties. If the dispute is not considered at ICSID, the foreign investor has the right to submit the dispute to any international arbitration body which has been set up by the United Nations Commission for International Trade Law (UNCITRAL) to resolve the dispute in accordance with the rules established under the arbitration and international agreement. Under the U.S.QGeorgia Bilateral Investment Treaty, investors have additional rights.

Georgia is party to the International Convention on the Recognition and Enforcement of Foreign Arbitration Awards. As a result, the Government agrees to accept binding international arbitration of investment disputes between foreign investors and the state. The Ministry of Justice was designated in December 2005 to oversee the governmentQs interests in arbitrations between the state and private investors.

It is recommended that contracts between private parties include a provision for international arbitration of disputes because of deficiencies in the Georgian court system. Litigation can take excessively long periods of time. There is a continuing concern about the adquacy of training of judges and about their susceptibility to pressure from the government or other outside influences.

Performance Requirements and Incentives

Performance requirements are not a condition of establishing, maintaining, or expanding an investment, but have been imposed on a case-by-case basis in some privatizations, for example, commitments to maintain employment levels or to make additional investments within a specified period of time. While many privatizations have proceeded smoothly and regularly, the current government has used non-fulfillment of performance requirements to justify rescinding privatizations and re-selling enterprises, usually for higher prices, sometimes to the benefit of other interested parties. Most types of performance requirements are prohibited by the U.S.-Georgia Bilateral Investment Treaty.

The Government of Georgia does not offer incentives to foreign investors, but relies on the many improvements it has made in the overall business climate to attract them to invest in the country.

Right to Private Ownership and Establishment

Foreign and domestic private entities may freely establish, acquire, and dispose of interests in companies and business enterprises, and engage in all forms of remunerative activity. Some specific laws regulate business activity in the banking, agribusiness, energy, transport, and tourism sectors. To the extent that public enterprises compete with private enterprises, they do on the basis of equality.

Foreign individuals and companies may buy non-agricultural land in Georgia. Only Georgian citizens or companies may buy agricultural land in their own name, but even agricultural land can be purchased by forming a Georgian corporation that may be up to 100 percent foreign-owned.

Investors should exercise extreme caution in purchasing property in Abkhazia and South Ossetia. Land for sale rightfully may belong to QAbkhazia and South Ossetia. Land for sale rightfully may belong to internally displaced persons forced to leave Abkhazia and South Ossetia in the early 1990s or 2008 and may have improperly been placed on the market by the de facto authorities of GeorgiaQs breakaway regions. The government of Georgia considers the sale of property in those regions illegal under Georgian law and property could be reclaimed by original owners at a future date.

Protection of Property Rights

Secured interests in both real and personal property are recognized and recorded. However, deficiencies in the operation of the court system can hamper investors from realizing their rights in property offered as security. Foreign investors' interests have sometimes been harmed by biased court proceedings and by legislation and decrees that clearly favor a Georgian entity or partner involved in the enterprise. Judicial reform has been identified as a top priority for the Georgian government since late 2005, but it will take some time for court and

legal reforms to bear fruit. It is recommended that contracts between private parties include a provision for international arbitration of disputes.

Disputes over property rights have undermined confidence in the impartiality of the Georgian judicial system and rule of law, and, by extension, GeorgiaQs investment climate. Both foreign and Georgian investors have expressed reservations about the competence, independence and impartiality of court decisions. In a few cases lower court decisions have changed control of property or of entire enterprises on questionable legal grounds or on the basis of forged documents. In some cases these decisions have been reversed by higher courts or government action, in others not.

Protection of Intellectual Property Rights

Georgia acceded to the WTO and the TRIPS agreement in 2000. In 2004, the Georgian parliament ratified the Rome Convention for Protection of the Rights of Performers, Producers of Phonograms and Broadcasting Organization, and the Lisbon Agreement on Denomination of Origin. In 2005, Georgia joined WIPO International Convention for the Protection of New Varieties of Plants. Georgia is a party to the Bern Convention, member of two WIPO digital treaties Q the Copyright Treaty and the Performance and Phonograms Treaty, The Hague Agreement and the Budapest Treaty Concerning the International Recognition of the Deposit of Microorganisms for the Purpose of Patent Procedures.

Six laws regulate intellectual property rights (IPR): the Law on Patents, Law on Trademarks, Law on Copyrights and Neighboring Rights, Law on Appellation of Origin and Geographic Indication of Goods, Law on Topographies of Integrated Circuits, and Law on IP-Related Border Measures. Georgian law now provides retroactive protection for works of literature, art and science, or sound recordings for 50 years.

While Georgia has brought its legislation into line with international standards, enforcement remains problematic. Pirated video and audio recordings, electronic games, and computer software are freely sold in Georgia. Use of unlicensed software in government offices and businesses is common. Internet service providers host websites loaded with unlicensed content. Responsibility for WTO compliance was recently been transferred to the Ministry of Economic Development, which still needs to develop its capacity in this regard. The Customs Department is developing a new Intellectual Property Objects Register to assist in identification of counterfeit goods at the border. Nevertheless, IPR awareness in the Department is low and hampered by frequent personnel changes. Further clarification of responsibilities between the Ministry of Internal Affairs and the Ministryof Finance is needed, as the MOIA has authority over some types of property rights protection and the Ministry of Finance over others. Judges and lawyers lack knowledge of IPR laws and understanding of IPR issues. GeorgiaQs Patent and Trademark Agency needs greater familiarity with emerging technologies.

Transparency of Regulatory System

The Georgian government has made a commitment to greater transparency and simplicity of regulation. Laws and regulations are published in Georgian in the official gazette, the Legislative Messenger. The number of taxes has been reduced from 22 to six. The tax on corporate profits is 15 percent. The Value Added Tax is 18 percent. The tax on personal income was set at a flat rate of 25 percent after a 2007 law increased the personal income tax and eliminated the employer-paid social tax on wages. In 2008, the Government of Georgia further Qsocial tax on wages. In 2008, the Government of Georgia further reduced the personal income tax rate from 25 percent to 20 percent and reduced the dividend income tax rate from ten to five percent. Both reductions took effect on January 1, 2009. This new initiative is an acceleration of legally binding commitments, made earlier, to reduce the personal income tax rate to 15 percent by 2013 and to further reduce the dividend income tax rate to zero by 2012. Legislation was passed in 2008 setting zero dividend and capital gains tax rates with respect to publicly traded equities (defined as having free float in excess of 25 percent). There are excise taxes on cigarettes, alcohol, and fuel. Imports are taxes at rates of zero, five, and 12 percent. Nearly all goods, except for some agricultural products, are taxed at the zero rate.

The Georgian National Investment and Export Promotion Agency has

established Business Information Centers in Tbilisi and other Georgian cities. These centers are intended to provide domestic and foreign businesses with a standard package of information relevant to doing business in Georgia. They also provide specific information according to the needs of individual businesses. The Business Information Centers are also conducting an ongoing public-private dialog to facilitate communication between regulators and the business community.

International accounting standards became binding for joint stock companies in Georgia as of January 1, 2000. For other institutions, such as banks, insurance companies and companies operating in the field of insurance, as well as limited liability companies, limited partnerships, joint liability companies, and cooperatives, the standards became binding on January 1, 2001. Private companies (excluding sole entrepreneurs, small businesses and non-commercial legal entities) are required to perform accounting and financial reporting in accordance with international accounting standards. Sole entrepreneurs, small businesses, and non-commercial legal entities perform accounting and financial reporting following simplified interim standards approved by the Parliamentary Accounting Commission. Despite the legal requirement, the conversion to international accounting standards is going slowly, in part because many businesses have operated in the shadow economy, or maintained two sets of books. Qualified accounting personnel are in short supply.

Efficient Capital Markets and Portfolio Investment

Banking was one of the fastest growing sectors in the Georgian economy from 2003-2008. However, growth slowed during 2008-2009 due to the Russia-Georgia conflict and the world financial crisis. The share of banking assets amounted to 42 percent of GDP in 2007 and is expected to reach 60 percent by the end of 2009. Currently, the banking system consists of domestically-based small- and medium-sized banks, a handful of large banking institutions based in Tbilisi with subsidiaries (HSBC, Societe Generale, Vneshtorgbank, Privat Bank, etc), and two foreign banks with branches (Turkish Bank Ziraat and the International Bank of Azerbaijan). In 2007, commercial bank assets grew by 70 percent with a profit growth of 65 percent. Total assets of the countryQs 19 commercial banks (16 of which have foreign capital) were $4.7 billion at the end of 3rd quarter of 2009. As of Q3 2009, commercial bank assets decreased by four percent compared to Q3 2008 and the net loss of commercial banks has doubled from -37m GEL in Q3 2008 to -82m GEL in Q3 2009.

Credit from commercial banks is available to foreign investors as well as domestic clients. Banks continue offering business, consumer, and mortgage loans. By the end of Q3, 2009 loans to individuals (41 percent) and loans to retailers/services (29 percent) had major shares in the total banking sector loan portfolio. In addition, the International Finance Corporation (IFC), European Bank for Reconstruction and Development (EBRD), U.S. Overseas Private Investment Corporation (OPIC), Millennium Challenge Corporation (MCC), and other international development agencies have a variety of lending programs that make credit available to large and small businesses in Georgia.

The limited number of foreign banks operating in Georgia reflects, in part, the small size of GeorgiaQs financial market. However, foreign investment in the sector is significant, accounting for 80 percent of total bank capital as of November 2009, per National Bank data. In 2005, Russian, Kazakhstani, U.S., and German capital was invested in Georgian banks. In September 2006, the French bank Societe Generale acquired 60 percent of one of the leading Georgian banks, Bank Republic. In 2007, British bank HSBC entered the Georgian market. UAE Dhabi Group acquired Standard Bank in 2008.

Georgian banks have remained solvent during the current global credit crisis largely due to the mandated 13 percent central bank reserve requirement and conservative lending practices. The Georgian central bank relaxed the reserve requirement to five percent in the aftermath Qbank relaxed the reserve requirement to five percent in the aftermath of the war and in response to the global credit crisis to try to inject liquidity into the market and spur new lending. The reserve requirement remains at five percent.

The law on commercial bank activities has been amended to improve the transparency of ownership and corporate governance of banks. In March 2006, the restriction under which one shareholder or a group of joint shareholders could hold no more than 25 percent of voting shares in a

bank was abolished. A new law regulating the activity of microfinance organizations came into force in August 2006.

The National Securities Commission of Georgia regulates the securities market. All joint stock companies with more than 50 shareholders -- currently about 1800 companies in Georgia -- are required to submit annual, semi-annual, and current reports prepared in accordance with internationally accepted accounting standards.

The Georgian Stock Exchange (GSE) is the only organized securities market in Georgia. Designed and established with the help of USAID and operating within the legal framework drafted with the assistance of American experts, GSE complies with global best practices in securities trading and offers an efficient investment facility to both local and foreign investors. The GSE automated trading system can accommodate thousands of securities that can be traded by brokers from workstations on the GSE floor or remotely from their offices. As of 2009, about 150 companies have access to GSE. 1887 trades (total value of approximately USD 58 million) were executed and reported in 2009 compared to 3180 trades (value of USD 160 million) in 2008.

No law or regulation authorizes private firms to adopt articles of incorporation or association that limit or prohibit foreign investment, participation, or control. QCross-shareholder" or "stable-shareholder" arrangements are not used by private firms in Georgia. Georgian legislation does not protect private firms from takeovers. There are no regulations authorizing private firms to restrict foreign partners' investment activity or limit foreign partners' ability to gain control over domestic enterprises.

Political Violence

Georgia suffered considerable instability in the immediate post-Soviet period. After independence in 1991, civil war and separatist conflicts flared up in the areas of Abkhazia and South Ossetia. The status of each region remains unresolved and the central government does not have effective control over these areas. The United States supports the territorial integrity of Georgia within its internationally-recognized borders. In August 2008, tensions boiled over culminating in a brief war between Georgia and Russia. Russia invaded and occupied portions of undisputed Georgian territory, destroyed portions of vital infrastructure, blocked the main east-west highway, and blockaded the Georgian port of Poti. Nearly all damaged infrastructure has been repaired and commerce has mostly returned to normal. While the separatist regions of South Ossetia and Abkhazia have declared independence, thus far only Russia, Venezuela, Nicaragua, and the small island country of Nauru have recognized them. Tensions still exist and reports of violence both inside the breakaway republics and near the administrative boundary lines are common, but other parts of Georgia, including Tbilisi, are not directly affected.

Corruption

Under President Saakashvili, Georgia has taken action to reduce corruption. Anti-corruption efforts have resulted in the arrests of former officials, the radical downsizing of state bureaucracies, and effective crackdowns on smuggling. Consequently, state revenue collections have increased about 50 percent. The notoriously corrupt traffic police were completely disbanded in mid-2004.

Articles 332-342 of the Criminal Code criminalize bribery. Georgian legislation provides for civil forfeiture of undocumented assets from public officials who are charged with corruption offenses. Bribery is a criminal act under Georgian law, and Parliament recently accepted a package of constitutional amendments that make abuse of public office a criminal offense with a maximum penalty of 15 years imprisonment and confiscation of property. Penalties for accepting a bribe start at six years in prison and can extend up to 15 years depending on the circumstances accompanying the offense. Penalties for giving a bribe can include a fine, a minimum prison sentence of two years, or both. In aggravating circumstances, when a bribe is given to commit an illegal act, the penalty can be from four to seven years. The definition of a public official includes foreign public officials and employees of international organizations and courts for purposes of such offenses as accepting a bribe, giving a bribe, and trading in influence. White collar crimes such as bribery fall under the investigative jurisdiction of the Prosecutor's Office.

The GovernmentQs Anti-Corruption Strategy calls for an effective state management system and legal and public feedback mechanisms to prevent corruption. Among the goals of the strategy are the identification and Qcorruption. Among the goals of the strategy are the identification and analysis of conditions conducive to corruption as well as elaboration of mechanisms for their eradication,strengthening of principles of accountability and public disclosure in the public sector, prosecution of lawbreakers, and facilitation of competitive development of the business sector.
Georgia also significantly improved in Transparency International's annual Corruption Perceptions Index, ranking 66 in 2009 out of 180 countries surveyed. In 2005, Georgia was ranked 130. The Index ranks countries in terms of the degree to which resident and non-resident businesspeople and country analysts perceive corruption to exist in the public and political sectors. Since the Rose Revolution, Georgia's score has steadily improved. In 2003 GeorgiaQs score in the index was 1.8, falling in a category of countries where corruption, according to TI, was Qperceived to be pervasive.Q In 2009 GeorgiaQs score was 4.1. This current score means that Georgia has moved out of the group of countries considered to have a "rampant corruption problem" (those under 3.0). In comparison with countries of the former Soviet Union, Georgia ranks well ahead of neighboring Armenia (120), Kazakhstan (120), Azerbaijan (143), Russia (146), and Ukraine (146).

Georgia reasserted central control over the Black Sea region of Adjara in May 2004, reducing illicit economic activity there. However, the lack of central government control and international access to Abkhazia and South Ossetia since the 2008 conflict means that smuggling levels cannot be monitored or estimated. The Georgian government has raised concerns with Russia and with the international community about continued high levels of smuggling, money laundering, and even counterfeiting of U.S. dollars in the areas outside its control.

Georgia is not a signatory to the Organization for Economic Co-operation and Development (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. Georgia has ratified the UN Convention against Corruption, however. Georgia cooperates with the Group of States Against Corruption (GRECO) and the OECDQs Anti-Corruption Network for Transition Economies (ACN). GRECO concluded in 2006 that Georgia had successfully implemented the first round of its anti-corruption recommendations. In 2003, ACN proposed an anti-corruption action plan and 21 recommendations for Georgia. In 2006, the OECD positively assessed the progress of anti-corruption measures and considered all but four of its recommendations implemented. OECD conducted an assessment of Georgia in October 2009 and will release the respective report in April 2010.

Bilateral Investment Agreements

Georgia has negotiated bilateral agreements on investment promotion and mutual protection with 31 countries, including the U.S., Armenia, Austria, Azerbaijan, Belgium, Bulgaria, China, Czech Republic, Estonia, Egypt, Finland, France, Germany, Greece, Iran, Israel, Italy, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Luxemburg, Moldova, Netherlands, Romania, Sweden, Turkey, Turkmenistan, Uzbekistan, the United Kingdom, and Ukraine. Internal procedures have been completed and drafts are being negotiated with the governments of India, Bangladesh, Croatia, Denmark, Norway, Philippines, Cyprus, Indonesia, Malta, and Iceland. Negotiations are underway with Belarus, Tajikistan, Slovenia, Estonia, Slovakia, Syria, Bosnia-Herzegovina, Switzerland, Korea, Kuwait, Lebanon, Portugal, Saudi Arabia, and Jordan. In 2007, Georgia signed a Trade and Investment Framework Agreement (TIFA) with the United States. Georgia is currently renegotiating its existing Bilateral Investment Treaty with the United States.

A free trade agreement is in force with the Commonwealth of Independent States, and others exist bilaterally with Ukraine, Russia, Kazakhstan, Azerbaijan, Armenia, Moldova, Turkmenistan, and Turkey. An agreement is signed, but not yet ratified, with Uzbekistan. Ongoing consultations on free trade are being held with the European Union, Belarus, Kyrgyzstan, Cooperation Council of Gulf Arab States, and Tajikistan.

OPIC and Other Investment Insurance Programs

From 1993 through 2007, OPIC has committed over USD 104 million in financing and political risk insurance to projects in Georgia. These

projects include the development of hotel and office space, production of pharmaceuticals, food processing and farming, cold storage, banking, mortgage lending, and financial leasing services. In 2008, as part of the United StatesQ response to help Georgia recover from the conflict with Russia, OPIC committed USD 176 million in financing. A large portion of OPICQs assistance will be used to underwrite mortgages aimed at allowing Georgian banks to offer smaller more affordable mortgages to the Georgian public. Other funding will support commercial and residential property development projects.

Labor

Georgia offers an abundant supply of skilled and unskilled labor at attractive costs compared not only to Western European and American Qattractive costs compared not only to Western European and American standards, but also to Eastern European standards. The labor force is among the best educated and most highly trained in the former Soviet Union. While some of the best qualified professionals and technicians emigrated from Georgia (mostly to Russia, the U.S., and Europe) after the Soviet Union's collapse, many have remained in the country or returned from abroad and are attempting to find a new role in GeorgiaQs market economy. Unemployment remains high and job creation has been a particular challenge.

The labor market in Georgia is one of the world's freest. Wage negotiations take place between employees and employers and trade unions are not powerful. Labor, health, and safety laws are not considered an impediment to investment. A new labor code which entered into force in June 2006 considerably liberalized labor regulations. The code defines the minimum age for employment (16), work hours (41 per week), annual leave (24 calendar days) and leaves the rest to be regulated by agreement between the employer and employee.

Payment of at least one monthQs salary is required if the employer initiates a dismissal. Employees must give one monthQs notice of intention to quit. No notice requirement is imposed on the employer prior to dismissal. Employees are entitled to up to 126 days (4 months) of maternity leave and, together with unpaid leave, up to 16 months. Under the new Labor Code, a contract of employment may bar an employee from using the knowledge and qualifications obtained while performing his duties with another employer. This provision may remain in force even after the termination of labor relations.

Since January 2008, employers are not required to pay social security contributions for employees. The former 12 percent income tax paid by employees and 20 percent social security tax paid by employers on their employees' wages was merged into a unified personal income tax at the rate of 25 percent in 2008, shifting the employer's tax burden to the employee. From January 2009, the overall effective tax rate paid by both self-employed persons and employees has been further reduced from 25 to 20 percent. The state social security system provides modest pension and maternity benefits. The minimum monthly pension is USD 44. The average monthly salary across the economy in the second quarter of 2009 was GEL 560 (USD 333). The minimum wage for government employees is GEL 115 (USD 69) per month. The minimum wage in the private sector has not changed in many years at GEL 20 (USD 12) per month, but few, if any, workers earn so little.

Georgia has signed multiple ILO agreements, including the Forced Labor Convention of 1930; the Paid Holiday Convention of 1936; the Anti-Discrimination (employment and occupation) Convention of 1951; the Human Resources Development Convention of 1975; the Right to Organize and Collective Bargaining Convention of 1949; the Equal Remuneration Convention of 1951; the Abolition of Forced Labor Convention of 1957; the Employment Policy Convention of 1964; and the Minimum Age Convention of 1973.

Foreign Trade Zones/Free Ports

In June 2007, the Parliament of Georgia adopted a law on free industrial zones, which defined the form and function of free industrial/economic zones. Financial operations in such zones may be performed in any currency and foreign companies operating in free industrial zones will be exempt from taxes on profit, property, and VAT. GeorgiaQs Ministry of Economic Development has allocated a 400 hectare area adjacent to the Black Sea Port of Poti for the first such zone. RAK Investment Authority (Rakeen group Q UAE based) purchased 100 percent of the shares of LLC Poti Sea Port, and pledged to develop a free economic zone on 300 hectares of land in Poti and to build a new

port terminal on a 100 hectare site. Construction of the new port terminal in Poti will start in the second half of 2010 and is expected to be finished by 2025. The first phase of construction should be finished by 2013, and will turn Poti Seaport into an international industrial zone with port, railroad, and other facilities. A second free economic zone has begun to function in the western Georgian city of Kutaisi. The Egyptian company Fresh Electric has established a factory as a part of the 27 hectare zone in which they are producing kitchen appliances. The company committed to build about one dozen textile-, ceramics-, and home appliance-producing factories in the zone, and investover USD 2 billion.

Foreign Direct Investment Statistics

Foreign Direct Investment (FDI) in Georgia dramatically increased during the periods of 1997-1998, 2003-2004, and 2006-2008. The first two peaks were related to the construction of the BakuQSupsa and Baku-Tbilisi-Ceyhan oil pipelines. FDI inflows in 2006-2007 hit historical highs due to privatization of state-owned enterprises and Qhistorical highs due to privatization of state-owned enterprises and the impact of economic reforms. FDI totaled USD 1.1 billion (15.3 percent of GDP) in 2006, more than doubling the 2005 total of USD 0.4 billion. FDI inflow in 2007 almost doubled again to USD 2.0 billion. Large FDI inflow in the first half of 2008 showed that investor interest in Georgia remained high, however, the August 2008 conflict with Russia undermined investor confidence and the subsequent global financial crisis further restricted FDI. Accordingly, total FDI in 2008 decreased to USD 1.3 billion.

Official statistics on FDI inflow from 2000-2009 are as follows (USD 1000):

2000	-131,200,000
2001	-109,800,000
2002	-167,400,000
2003	-339,400,000
2004	-499,100,000
2005	-449,800,000
2006	-1,190,400,000
2007	-2,014,800,000
2008	-1,293,700,000
2009*	- 505,200,000

Breakdown of FDI by major investor countries (USD 1,000Qs):

	2007	2008	2009*
ArmeniaQ	-4,895	-15,061	-6,432
Azerbaijan	41,368	23,943	7,827
China	6,877	-2,271	-369
Cyprus	148,644	26,166	12,707
Czech Republic	227,926	34,858	11,431
Denmark	158,126	256	-49
Egypt	-	-	115,000
Kazakhstan	88,486	65,942	912
Netherlands	299,277	135,870	46,159
Panama	6,178	-2,470	61,116
Russia	88,997	26,212	13,402
Turkey	93,871	164,526	71,542
United Arab Emirates	130,859	306,576	144,938
United Kingdom	145,475	148,908	41,474
USA	84,412	167,921	-46,272
Virgin Islands, British	187,816	156,847	1,280

Breakdown of FDI by economic sectors (USD 1,000s):

	2007	2008	2009*
Agriculture	15,528	7,844	4,940
Industry	398,241	207,328	143,886
Energy sector	362,581	294,865	30,146
Construction	171,892	56,725	65,727
Transport and communications	416,695	422,690	29,305
Real estate	30,544	277,838	103,557
Other services	382,807	283,165	117,773
Banking system	136,915	8,519	7,555

* - FDI through the first three quarters of 2009

Source: Statistics Department of Georgia

The United Arab Emirates, the United States, and Turkey topped the list of foreign investor countries in 2008. The Virgin Islands, the United Kingdom, and the Netherlands ranked next. For the first three quarters of 2009, United Arab Emirates was again the top foreign investor in Georgia at USD 145 million, followed by Egypt (USB 115m), Turkey (USD 72m), and Panama (USD 61m).

The drop in FDI is tempered by the fact that as of November 2009, Georgia received or entered into agreements for USD 2.1bn of the USD 4.5bn pledged at the Brussels donor conference in October 2008. The pledged or received amount corresponds to approximately 19 percent of 2009 estimated GDP, according to goverment data. However, the government foresaw yet another upward trend in FDI in 2010, expecting foreign invenstments to top the USD 2 billion target due to interest expressed by Egyptian and Qatari businesses.

The U.S. has been one of the largest foreign investors in Georgia since ¶1999. U.S. investors accounted for 30 percent of FDI in Georgia in 2000, 21 percent in 2001, and 49 percent in 2002. In 2003 and 2004, the U.S. share decresed to 21 and 16 percent, respectively, and dropped to 3 percent in 2005. This decline can be attributed to the completion of large pipeline projects as well as increased inflow of capital from other countries. In 2006, U.S. investment accounted for 15 percent of the total, but only 4 percent in 2007 and 11 percent in 2008.

Of note is the United Arab Emirates' increased interest in Georgia, evident in the investments of the Rakeen and Dhabi Groups in the port, real estate, banking, and other sectors.

The Georgian Government is actively promoting investment in Georgia, and has held a series of investment road shows around the world. End Text.

BASS